

STATE OF NEW YORK
DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
JOHN KYPREOS, OFFICER OF	:	DETERMINATION
TRI-STATE ALUMINUM PRODUCTS, INC.	:	DTA NO. 4731
	:	
for Revision of a Determination or for Refund of Sales and	:	
Use Taxes under Articles 28 and 29 of the Tax Law for the	:	
Period June 1, 1988 through February 29, 1992.	:	

Petitioner, John Kypreos, officer of Tri-State Aluminum Products, Inc., 2316 Legion Street, Bellmore, New York 11710-4911, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1988 through February 29, 1992.

On October 9, 1996 and October 21, 1996, respectively, petitioner, by Stewart Buxbaum, CPA, and the Division of Taxation, by Steven U. Teitelbaum, Esq. (John E. Matthews, Esq., of counsel), waived a hearing and agreed to submit this matter for determination based upon documents and briefs. All documents and briefs were to be submitted by February 7, 1997, which date began the six-month period for issuance of this determination. After a review of the evidence and arguments submitted, Thomas C. Sacca, Administrative Law Judge, renders the following determination.

ISSUES

I. Whether the Division of Taxation properly resorted to a test period audit method to determine Tri-State Aluminum Products, Inc.'s sales and use tax liability.

II. Whether petitioner has shown error in either the audit method or result.

FINDINGS OF FACT

Petitioner, John Kypreos, was the president of Tri-State Aluminum Products, Inc. ("Tri-State"), which did business under the name Tri-State Window Factory. The business, located at 355 Marcus Boulevard, Deer Park, New York 11729, was involved in the manufacture and

installation of custom windows.

On August 29, 1994, following an audit of Tri-State's books and records, the Division of Taxation ("Division") issued a Notice of Determination of sales and use taxes due against petitioner, as officer of Tri-State, covering the period June 1, 1988 through February 29, 1992, for taxes due of \$293,228.82, plus interest.

The Division began the audit by mailing to Tri-State a standard form audit appointment letter dated October 17, 1991. In addition to setting a date and time for the first meeting between Tri-State and the Division's auditor, this letter specifically requested that Tri-State make available at the time of the first meeting all books and records pertaining to Tri-State's sales tax liability for the period under review. The letter indicated that the period under review was September 1, 1988 through August 31, 1991. In the letter, the Division requested that the corporation make available for the auditor all journals, ledgers, sales invoices, purchase invoices, cash register tapes, Federal income tax returns, exemption certificates, guest checks and bank statements maintained for the audit period.

On May 4, 1992, the Division sent a second appointment letter to Tri-State requesting the same documentation. In this letter, however, the period under review was extended to June 1, 1988 through February 29, 1992.

All of the requested records were made available to the auditor by Tri-State. The auditor concluded that the records provided an opportunity to trace any transaction back to the original source or forward to a final total. The accounting records were considered by the auditor to be in an auditable condition. The gross sales per the records of Tri-State were in substantial agreement with the sales as reported on its Federal income tax returns, and the purchases per Tri-State's records were in substantial agreement with purchases as reported on its Federal income tax returns. Finally, according to the auditor, the business operation had adequate internal control procedures.

The auditor conducted an analysis of Tri-State's sales for a two-week period in November 1991 which revealed that all of the corporation's sales were capital improvements.

Properly completed capital improvement certificates had been obtained by Tri-State for all jobs performed. As a result of this review, the auditor concluded that all of Tri-State's sales consisted of capital improvements and were thus exempt from the imposition of sales tax. The auditor then turned his attention to the corporation's purchases. In that Tri-State had complete and adequate books and records, the auditor had Tri-State, by petitioner, as president, execute on May 20, 1993 a Test Period Audit Method Election Form which stated that the audit of recurring expense purchases would be conducted using the test period audit method.

The auditor first analyzed the material expense account for the period March 1, 1991 through May 31, 1991. This review revealed that Tri-State was not properly paying tax on its purchases used in the capital improvement jobs. An error rate of 74.85% was initially calculated, but after discussions with Tri-State's representative about suppliers to whom tax was paid but not indicated in the test, the error rate was adjusted to 70%. The additional tax due on the material expense account was determined to be \$229,863.31.

An analysis of the manufacturing expense account for the same period revealed the same result; that Tri-State was not properly paying tax on purchases it was using in capital improvements. The auditor computed an error rate of 99.80% which resulted in additional tax due of \$57,065.19.

The auditor analyzed Tri-State's office expense account for the months of May, July and October 1991. An error rate of 17.9% was computed resulting in additional tax due of \$547.37.

A review of Tri-State's purchases of electricity and gas revealed that Tri-State was improperly claiming an exemption from sales and use tax. As Tri-State's consumption of electricity and gas was not predominantly used in the manufacturing process, it was subject to the imposition of sales and use tax. The additional sales and use tax due on its purchases of electricity and gas was \$4,827.52.

In sum, the total amount of expense purchases determined by the auditor to be subject to sales and use tax was \$3,744,933.00, resulting in additional sales and use tax due of \$292,303.39.

An analysis by the auditor of Tri-State's asset account revealed \$12,339.00 in assets purchased with respect to which Tri-State was unable to verify payment of sales tax upon purchase. The failure of Tri-State to substantiate that tax was paid resulted in additional tax determined to be due of \$925.43.

During the audit, Tri-State, by petitioner, as president, executed five consents extending the period of limitation for assessment of sales and use taxes under Articles 28 and 29 of the Tax Law which collectively extended to September 20, 1994 the period within which the Division could assess tax due for the period June 1, 1988 through May 31, 1991.

On December 29, 1995, the Bureau of Conciliation and Mediation Services ("BCMS") issued a Conciliation Order reducing the tax due to \$52,282.07 by eliminating all but the last three quarters of the notice of determination as the consents extending the period of limitation for assessment of sales and use taxes related only to the corporation and not to petitioner.

CONCLUSIONS OF LAW

A. Every person required to collect tax must maintain and make available for audit upon request records sufficient to verify all transactions in a manner suitable to determine the correct amount of tax due (Tax Law § 1135[a]; 20 NYCRR 533.2[a]). Failure to maintain and make available such records, or the maintenance of inadequate records, will result in the Division of Taxation's estimating tax due (Tax Law § 1138[a]). To determine the adequacy of a taxpayer's records, the Division of Taxation must first request and thoroughly examine the taxpayer's books and records for the entire period of the proposed assessment (Matter of Adamides v. Chu, 134 AD2d 776, 521 NYS2d 826, 828, lv denied 71 NY2d 806, 530 NYS2d 109; Matter of King Crab Rest. v. State Tax Commn., 134 AD2d 51, 522 NYS2d 978, 980). The purpose of such an examination is to determine whether the records are so insufficient as to make it "virtually impossible to verify taxable sales receipts and conduct a complete audit" (Matter of Chartair, Inc. v. State Tax Commn., 65 AD2d 44, 411 NYS2d 41, 43). When estimating sales tax due, the Division must adopt an audit method that will reasonably calculate the amount of taxes due (see, Matter of W.T. Grant Co. v. Joseph, 2 NY2d 196, 159 NYS2d 150, 157, cert denied 355

US 869). Whether the audit method used was reasonably calculated to reflect the taxes due can only be determined based on information made available to the auditor before the assessment is issued (Matter of Queens Discount Appliances, Tax Appeals Tribunal, December 30, 1993; Matter of House of Audio of Lynbrook, Tax Appeals Tribunal, January 2, 1992). The burden rests with the taxpayer to show by clear and convincing evidence that the methodology was unreasonable or that the amount assessed was erroneous (Matter of Meskouris Bros. v. Chu, 139 AD2d 813, 526 NYS2d 679, 681; Matter of Surface Line Operators Fraternal Org. v. Tully, 85 AD2d 858, 446 NYS2d 451, 453).

B. The record in this case clearly shows that petitioner maintained and made available upon the Division's requests records sufficient to verify its sales and purchases for the period under review. The Division was therefore not authorized under Tax Law § 1138(a) to estimate petitioner's sales and use tax liability. In accordance with this restriction, the Division obtained from Tri-State a Test Period Audit Method Election Form signed by petitioner as president, which permitted the Division to perform a test period audit method on the corporation's recurring expense purchases. Prior to performing the audit on various purchase categories, the auditor reviewed Tri-State's sales for a two-week period in November 1991 to determine the type of sales made by the corporation. The review determined that all of Tri-State's sales were capital improvements and that the corporation had obtained a properly completed capital improvement certificate for each of the jobs.

Petitioner contends that it was improper for the auditor to use the two-week period in November 1991 to determine the type of sales that Tri-State transacted because the business had adequate and complete books and records and the audit method election form related only to purchases. Petitioner cites in support of his position Matter of Chartair, Inc. v. State Tax Commn. (*supra*), Matter of King Crab Rest. v. State Tax Commn. (*supra*), and Tax Law § 1138(a)(1). The reason for the requirement that the Division utilize the taxpayer's records in determining the amount of tax actually due is that "[t]he honest and conscientious taxpayer who maintains comprehensive records as required has a right to expect that they will be used in any

audit to determine his ultimate tax liability" (Matter of Chartair, Inc. v. State Tax Commn., supra). Here, because Tri-State had complete books and records, the auditor performed a detailed analysis of the corporation's purchases for a three-month period pursuant to a properly executed Test Period Audit Method Election Form. There was no test period audit method used by the Division to determine the corporation's sales and use tax due except that allowed by the election form. The review of sales for the two-week period in November 1991 was to determine the business operation of the corporation, so as to direct the auditor to either sales or purchases. No tax liability arose from this two-week review, and such review was therefore not in violation of the requirement that the corporation's books and records be reviewed in detail because of the adequacy of those records.

C. Petitioner's contention that the test performed of purchases was invalid due to the elimination at BCMS of certain of the quarters assessed (see, Finding of Fact "9"), including the period tested, resulting in the quarters tested being outside the periods remaining at issue, is without merit. The consent executed by the corporation did not limit the Division to any particular test period. Furthermore, the Division may determine tax due for one period based upon data projected from a different period (Matter of Markowitz v. State Tax Commn., 54 AD2d 1023, 388 NYS2d 176, affd, 44 NY2d 684, 405 NYS2d 454; Matter of Burbacki, Tax Appeals Tribunal, February 9, 1995). Therefore, the Division's use of the period initially preceding the periods remaining at issue was proper (see, Wallach v. Tax Appeals Tribunal, 206 AD2d 696, 614 NYS2d 647).

D. When the Division has the authority to use a test period audit method, it must use a method that is reasonably calculated to reflect the taxes due (Wallach v. Tax Appeals Tribunal, supra). As the Division did a detailed audit of the corporation's actual purchases pursuant to a properly executed Test Period Audit Method Election Form, the method was reasonable (Pallette Stone Corp. v. Guyer Builders, Inc., 212 AD2d 862, 622 NYS2d 127). Because the audit method selected was reasonable, it was incumbent upon petitioner to establish by clear and convincing evidence that the tax assessed herein was erroneous (see, Matter of Meskouris

Bros. v. Chu, supra).

It is undisputed that petitioner did not provide any documentation to establish that some of the capital improvement work performed by the corporation was done for government entities or other tax exempt organizations, as petitioner implies. Petitioner should have produced the sales invoices and the related tax exempt certificates to verify such claimed sales. Therefore, it must be concluded that petitioner has failed to establish by clear and convincing evidence that the amount of the tax assessed was erroneous (see, Cook v. Tax Appeals Tribunal, 222 AD2d 962, 635 NYS2d 355).

E. The petition of John Kypreos, as officer of Tri-State Aluminum Products, Inc., is denied and the notice of determination, dated August 29, 1994, is sustained.

DATED: Troy, New York
July 17, 1997

/s/ Thomas C. Sacca
ADMINISTRATIVE LAW JUDGE